The Manufacturers Hanover
Financial Digest
Economic Commentary, Selected Financial Data, and Business Indicators

MONDAY, OCTOBER 27, 1986 VOLUME XXIII, NUMBER 23

10/29/86 B5350-2

The Consumer . . .

Consumer spending has long been the dominant force behind the current business expansion, and this year is no exception. Over the past three quarters, growth in personal consumption expenditures has counteracted the weaknesses in other sectors of the economy. For example, while the inflation-adjusted gross national product increased at an annual rate of only 2.2 percent in the January-September period, real personal consumption expenditures climbed by a healthier 5.6 percent annual rate. In the third quarter of 1986, real consumer spending bolted upward at a 7.2 percent clip—three times as fast as the 2.4 percent rise posted by the real GNP. This disparity has raised concerns in some quarters that consumers may be living beyond their means. Indeed, if they are financially tapped out, any retrenchment in their spending could put a damper on this business expansion, which is now concluding its fourth year.

At first glance, consumers do appear to be overextended. Since spending has risen faster than after-tax income so far this year, consumers have dipped into their savings or resorted to buying on credit. As a result, the savings rate—savings as a percent of disposable income—is now 1.9 percent, the lowest rate in at least 35 years, while consumer credit outstanding compared with take-home income has reached a record 19.3 percent. These aggregate figures, however, mask a more positive picture of consumer finances.

For example, the savings rate number most often quoted may be somewhat misleading because of the methodology used to calculate the level of savings. The Commerce Department estimates disposable personal income and personal consumption expenditures and derives savings as the difference between the two. This method, however, does not make any adjustment to spending when purchases are made on credit. For example, in computing personal outlays, the total dollar amount of new cars sold is included, although only 25 percent of all new cars sold are paid in full at the time of the purchase. The other 75 percent are bought on credit.

This factor becomes important in light of the strong sales of new cars in August and September. The cut-rate financing offered by automakers to clear out high inventories of unsold 1986 models spurred an extraordinary jump in sales in August and September. If these unusual increases in car sales were excluded, the savings rates in August and September would rise to a more typical 3.8 percent and 3.7 percent, respectively. Moreover, if the dollar amount spent on new cars that was obtained through financing is taken out of consumption expenditures, the savings rate for both months would jump even higher.

. . . Appears Still Able . . .

In the case of consumer debt, in the past the upward climb of the ratio of outstanding installment debt to disposable income might have suggested that consumers were becoming overextended. Not this time. This is because much of the debt accumulated in recent years has been taken on by those high-income households which are probably best able to service it. According to Federal Reserve estimates, almost 50 percent of consumer installment debt outstanding is owed by households in the top income quintile. This proportion represents a substantial increase from 1977 when the richest households held 36 percent of such debt, and from 1970 when they accounted for only 22 percent. Add to this the fact that credit cards are used increasingly for convenience rather than for borrowing, with the holder often paying off the entire balance each billing period, and the actual burden of outstanding debt diminishes even further.

Already, consumers are cutting back on credit use without any dampening effects on their purchases. So far this year, consumers have taken on less than $42 billion in installment loans compared with $52.5 billion during the same period of last year. This was the smallest such increase in three years. Yet at the same time, retail sales rose 8.8 percent, compared with 7.5 percent last year. In August alone, the rise in consumer credit was a modest $3.7 billion. While auto credit accounted for two-thirds of this increase, its growth slowed to a mere $2.5 billion compared with an average increase of $3.5 billion in the preceding three months. This is somewhat puzzling in view of the fact that August car sales soared in response to new incentives

Copyright 1986
Manufacturers Hanover
270 Park Avenue, New York, N.Y. 10017

offered by automakers. It may indicate that many buyers either opted for cash rebates which reduced the amount of credit needed, or took the higher interest rate loans which allowed them more time to repay.

. . . To Keep The Expansion Going

Although the total level of indebtedness is certainly a consideration, it is the monthly repayments of such obligations in relation to disposable income which determine the true burden on consumers. Longer loan payback periods, lower interest rates, and growth in overall household assets have contributed to easing the burden of monthly installment payments, despite the very rapid growth in total installment debt over the last several years. According to a new study by the Federal Reserve, the ratio of consumer installment debt to disposable income was 24 percent higher in the first quarter of this year than in the first quarter of 1975. However, the ratio of debt service payments to disposable income was four percent lower.

The lengthening of maturities on many types of loans since 1975 accounts for much of this difference between the growth patterns of consumer installment debt and debt service payments. For example, the average maturity of new car loans issued by finance companies increased from 38 months in 1975 to 52 months in 1985. Clearly, an increase in maturity can decrease the scheduled monthly repayments of principal, even as it raises aggregate debt outstanding. If maturities had not increased, the consumer installment debt ratio

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 10/22/86	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	197.934	+ 2.269	+18.567
Loans to Depository Inst.	.888	+ .235	− .413
Float	.601	− .145	− .268
Total Reserve Bank Credit	216.068	+ 2.323	+20.500
Treasury Deposits with Federal Reserve Banks	3.552	+ .851	− .098
Currency in Circulation	202.763	− .294	+13.362
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	164.010	− .109	+41.101
	10/22/86		
Member Bank Reserves:			
Total Reserves Held	52.581	+ .814	+ 8.311
Excess (Deficiency)	.775	− .074	− .018
Net Free Reserves	.492	− .188	+ .169

Monetary Aggregates†		% Change Since Three Months Ago*	% Change Since Year Ago
M1 (10/13/86)	696.5	+ 15.6‡	+ 13.7‡
M2 (September '86)	2,741.3	+ 10.6	+ 8.4
M3 (September '86)	3,425.2	+ 10.3	+ 8.7
Domestic Nonfinancial Debt (2nd Q'86)	7,181.0	+ 11.5	+ 13.1

†Seasonally adjusted.

*Seasonally adjusted annual rate.
‡Four-week moving average.

New York Money Market

Offering Rates 10/24/86	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	5.30%	5.38%	5.48%
* Federal Agencies	5.45	5.51	5.60
* Municipal Notes—High Grade (46% Taxable Equivalent)	5.74	6.02	7.04
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	5.75	5.75	5.90

‡Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	5.50%	Nov.	5.70%
15- 29 days	5.65	Dec.	5.65
30- 59 days	5.75	Jan.	5.65
60- 89 days	5.70	Feb.	5.61
90-179 days	5.70	Mar.	5.60
180-239 days	5.60	Apr.	5.58
240-270 days	5.60		

‡Industrial Paper—Prime			
30- 89 days	5.73%	†Federal Funds Effective Rate	5.80%
90-120 days	5.67		

‡Discount basis. *Subject to availability. †Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'86n	$ 4,234	$ 4,176	$ 4,031
Gross National Product (1982 Dollars)*	3rd Q'86n	$ 3,683	$ 3,661	$ 3,604
Percent Change, Annual Rate	3rd Q'86n	2.4	0.6	4.1
Change in Consumer Prices*	Sep '86n	3.6%	2.4%	2.4%
Change in Producer Prices*	Sep '86	4.8%	3.6%	− 7.2%
Civilian Employment (Thousands of Persons)†	Sep '86	109,891	110,155	107,519
Unemployment as % of Civilian Labor Force†	Sep '86	7.0%	6.8%	7.1%
Personal Income*	Sep '86n	$ 3,512	$ 3,500r	$ 3,334
Leading Indicators Composite Index (1967=100)†	Aug '86	179.1	179.5	169.8
Industrial Production Index (1977=100) †	Sep '86n	125.3	125.1r	124.3
Change in Consumer Installment Credit †	Aug '86	$ 3.74	$ 5.56	$ 6.05
U.S. Merchandise Trade Balance	Aug '86	−$ 13.32	−$ 16.06	−$ 12.89
Plant and Equipment Expenditures*	4th Q'86	$383.99(a)	$380.52(a)	$397.88
Private Housing Starts (Thousands of Units)*	Sep '86n	1,680	1,818r	1,653
New Construction Expenditures*	Aug '86	$ 382.2	$ 378.1	$ 353.3
Total Business Inventories †	Aug '86n	$ 591.9	$ 591.9r	$ 579.5
Total Business Sales †	Aug '86n	$ 429.1	$ 427.5r	$ 428.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

would have risen only eight percent between the first quarters of 1975 and 1986 rather than the actual 24 percent, and the debt service payment ratio would have increased three percent instead of falling four percent.

Households' wealth is also a crucial determinant of consumption patterns. In the first half of this year, household financial assets, which include demand deposits, savings accounts, and stocks and bonds increased at a seasonally adjusted annual rate of 17.5 percent. At the same time, household liabilities, which include mortgages as well as installment debt and other outstanding loans, rose at only an 8.3 percent annual rate. By better managing their funds, consumers have enhanced their balance sheets. Households now hold $3.35 in financial assets for each dollar of their debt outstanding, the highest such ratio in ten years.

More good news comes from the inflation front. In the past 12 months, consumer prices rose a modest 1.7 percent, enabling consumers to enjoy increased buying power from their take-home pay. These modest increases in prices also helped to push the discomfort index, which measures the sum of unemployment and inflation rates, down to 8.5 percent in the third quarter—the lowest in more than 17 years. Thus, it is not surprising that consumer attitudes are brightening just in time for the Holiday shopping season. The Conference Board reported that consumer confidence, which sagged during the summer months, moved higher in September. H

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (10/8/86)	153,764	+ 48	– 5,325
New York City (10/15/86)	33,487	+ 58	+33,456
Commercial Paper (10/15/86)	330,667	+ 810	+45,993

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (10/8/86)	258,906	– 737	+ 4,463
New York City (10/15/86)	58,850	+ 512	+ 59,947

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (10/8/86)	747,304	– 6,457	+ 49,919
New York City (10/15/86)	163,182	+ 1,485	+ 152,424

Financial Markets

	Friday 10/24/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	5.38%	+ .05	– 1.85
180-Day Bills†	5.53	+ .04	– 1.88
Longest Bills†	5.75	+ .08	– 1.74
Recent Issues:			
6 3/8s 10/31/88 (When Issued)	6.31	+ .07	
6 3/4s 9/30/90	6.55	– .22	
7 3/8s 5/15/96	7.42	– .12	
7 1/4s 5/16/16	7.74	– .09	
Municipals:			
Bond Buyer–20 Bond Index* (10/23/86)	7.11%	+ .03	– 1.84
Blue List Total ($ Million)	$1,568	–$ 11	– $ 138
30-Day Visible Supply ($ Million)	$2,094	–$ 595	– $2,267
Total	$3,662	–$ 606	– $2,405
Corporates:			
Moody's Aa Composite (10/23/86)	9.33%	– .04	– 2.07
30-Day Visible Supply ($ Million)	$5,242	+$1,687	+ $ 881
Stocks:			
Dow-Jones Averages:			
Industrials	1,832.26	– 4.78	+ 475.74
Transportation	825.00	+ 1.12	+ 175.42
Utilities	202.27	+ 1.21	+ 43.11
65 Stocks	725.43	– .12	+ 175.30
N.Y.S.E. Composite Index	137.27	– .21	+ 28.91
N.Y.S.E. Avg. Daily Vol. for Week (000's)	127,032	+ 7,602	+ 16,220

* 46% Taxable equivalent 13.17%.

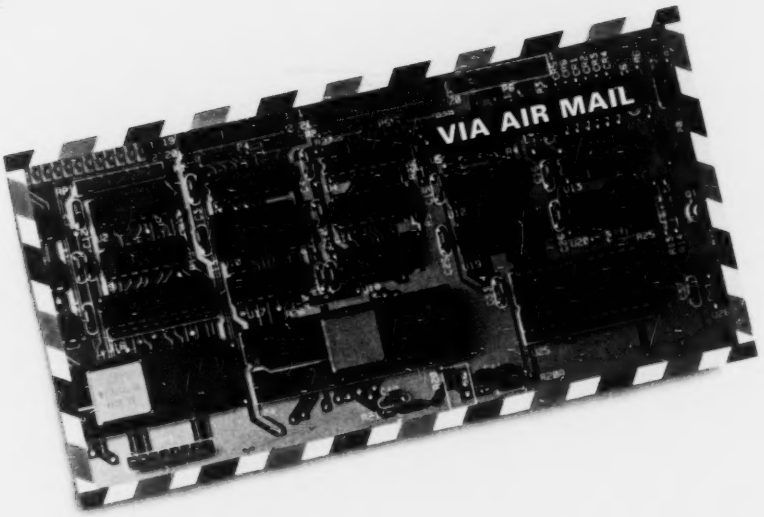
† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 10/24/86	Week Ago
Overnight	5.75%	5.75%
1 month	5.94	5.88
3 month	5.94	5.88
6 month	5.94	5.88
1 year	6.06	6.06
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.50%	7.34%
Long Term (7 to 15 yrs.)	8.44	8.22

FOREIGN EXCHANGE SPOT RATES

New York Opening (10/24/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02388	41.88
Canada	.7199	1.3890
Denmark	.1313	7.6175
France	.1513	6.6100
Germany	.4948	2.0210
Italy	.0007153	1398.00
Japan	.006211	161.00
Mexico	.001242	805.00
Netherlands	.4381	2.2825
Switzerland	.5993	1.6685
U.K.	1.4145	.7070



The Letter of Credit Comes of Age.

For generations, there was not much change in the way importers handled their L/C's. From sending an application to checking on a transaction's status, the process of paperwork and phone calls could take days to complete.

Now Manufacturers Hanover Trust is bringing the L/C into the electronic age with the Electronic Letter of Credit Service. Allowing you to prepare and transmit letter of credit transactions directly to us via Personal Computer. And obtain up-to-the-instant computer reports on your letter of credit activity. Swiftly. Accurately. Securely.

With our Electronic Letter of Credit Service your instructions are acknowledged in seconds, and processed without delay. Opening the way to an early delivery of your shipment—and a savings in time and money.

You can track the status of your L/C's and acceptances through our on-line inquiry capability. A unique feature of which allows you to generate reports in standard formats or to design your own.

Add to all of this the assurance that our dedicated team of trade professionals stands ready to give you prompt answers to all your questions.

So put some byte into your L/C with our Electronic Letter of Credit Service. It's one of a number of products that is opening up a new age in banking.

MANUFACTURERS HANOVER

Member FDIC

©1986 Manufacturers Hanover. All Rights Reserved.

The Manufacturers Hanover
Financial Digest
Bank Window, Church St. Station
New York, New York 10015

First Class Mail
U.S. Postage
PAID
New York, N.Y.
Permit No. 585

208 208006990 C 939 CONGR0001
SRI ACQUISITIONS
CONGRESSIONAL INFORMATION
SERVICE, INC.
4520 EAST-WEST HWY., SUITE 800
WASHINGTON, DC 20014